



Mr. D.P Msibi  
Municipal Manager  
Umjindi Local Municipality  
Box 33  
Barberton  
1300

14 December 2012

Reference: 02054REG11-12

Dear Sir

**Report of the Auditor-General on the financial statements and other legal and regulatory requirements of Umjindi Local Municipality for the year ended 30 June 2012**

1. The above-mentioned report of the Auditor-General is submitted herewith in terms of section 21(1) of the Public Audit Act of South Africa read in conjunction with section 188 of the Constitution of the Republic of South Africa [section 121(3) of the Municipal Finance Management Act of South Africa (MFMA)/ section 40(2) (departments) of the Public Finance Management Act of South Africa (PFMA)]
2. We have not yet received the other information that will be included in the annual report with the audited financial statements and have thus not been able to establish whether there are any inconsistencies between this information and the audited financial statements and the reported performance against pre-determined objectives. You are requested to supply this information as soon as possible. Once this information is received it will be read and should any inconsistencies be identified these will be communicated to you and you will be requested to make the necessary corrections. Should the corrections not be made we will amend and reissue the audit report.
3. In terms of section 121(3) of the MFMA you are required to include the audit report in the municipality's annual report to be tabled.
4. Until the annual report is tabled as required by section 127(2) of the MFMA the audit report is not a public document and should therefore be treated as confidential.
5. Prior to printing or copying the annual report which will include the audit report you are required to do the following:
  - Submit the final printer's proof of the annual report to the relevant senior manager of the Auditor-General of South Africa for verification of the audit-related references in the audit report and for confirmation that the financial statements and other information are those documents that have been read and audited. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.
  - The signature *Auditor-General* in the handwriting of the auditor authorised to sign the audit report at the end of the hard copy of the audit report should be scanned in when preparing to print the report. This signature, as well as the place and date of signing and the Auditor-General of South Africa's logo, should appear at the end of the report, as in

the hard copy that is provided to you. The official logo will be made available to you in electronic format.

6. Please notify the undersigned Deputy Business Executive well in advance of the date on which the annual report containing this audit report will be tabled.
7. Your cooperation to ensure that all these requirements are met would be much appreciated.

Kindly acknowledge receipt of this letter.

Yours sincerely

Signed



Sibongile Lubambo: [Mpumalanga]

Enquiries: Phetego Mokgope

Telephone: (013) 756 0800

Fax: (013) 756 0879

## **REPORT OF THE AUDITOR-GENERAL TO THE MPUMALANGA PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE UMJINDI LOCAL MUNICIPALITY**

### **REPORT ON THE FINANCIAL STATEMENTS**

#### **Introduction**

1. I have audited the financial statements of the Umjindi Local Municipality set out on pages xx to xx, which comprise the statement of financial position as at 30 June 2012, the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

#### **Accounting officer's responsibility for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2011 (Act No. 6 of 2011) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

#### **Auditor-General's responsibility**

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified audit opinion.

## **Basis for qualified opinion**

### **Accumulated surplus**

6. A disclaimer of opinion was issued on the prior year's financial statements. I was unable to determine the extent of the effect of these limitations on the balances as at 30 June 2012.

### **Property, plant and equipment**

7. The municipality could not provide me with sufficient appropriate audit evidence to support the assumptions made that a process had been performed to reassess the useful lives of assets and depreciate property, plant and equipment amounting to R24 581 585.
8. The municipality unbundled assets as per the requirements of GRAP 17. The municipality used the valuation roll as a basis for land and buildings. The valuation roll did not contain the latest fair values for assets, as it was prepared in prior years and did not make a distinction between land and buildings for certain properties. I could thus not rely on the amount disclosed under land and buildings to the value of R103 941 881 (2011: R103 813 594), as disclosed in note 5 to the financial statements. Consequently, I was unable to determine whether any adjustment relating to land and buildings in the financial statements was necessary.
9. The municipality could not provide sufficient appropriate audit evidence to support journal entries of R129 231 080 processed to property, plant and equipment.
10. The municipality's records did not permit the application of alternative procedures. Consequently, I could not obtain sufficient appropriate audit evidence as to the valuation, existence and completeness of the closing balance of property, plant and equipment amounting to R697 873 063 (2011: R687 381 987), as disclosed in note 5 to the financial statements.
11. A disclaimer of opinion was issued on the prior year's financial statements. I was unable to determine the extent of the effect of these limitations on the balances as at 30 June 2012.

### **Investment property**

12. The municipality unbundled assets as per the requirements of GRAP 17. The municipality used the valuation roll as a basis for valuating investment property. The valuation roll did not contain the latest fair values for assets, as it was prepared in prior years and did not make a distinction between land and buildings for certain properties. I could thus not rely on the amount disclosed under investment property to the value of R107 213 050 (2011: R119 035 000), as disclosed in note 4 to the financial statements. Consequently, I was unable to determine whether any adjustment relating to investment property in the financial statements was necessary.
13. The municipality could not provide me with sufficient appropriate audit evidence to support adjustments made to opening balances for investment property. I could not verify the validity, accuracy and completeness of the adjustment amounting to R5 105 950. I could thus not rely on the amount disclosed under investment property to the value of R107 213 050 (2011: R119 035 000), as disclosed in note 4 to the financial statements. Consequently, I was unable to determine whether any adjustment relating to investment property in the financial statements was necessary.

14. The municipality could not provide sufficient appropriate audit evidence to support journal entries of R11 821 950 processed to investment property.
15. The municipality's records did not permit the application of alternative procedures. Consequently, I could not obtain sufficient appropriate audit evidence as to the valuation, existence and completeness of the closing balance of investment property amounting to R107 213 050 (2011: R119 035 000), as disclosed in note 4 to the financial statements, respectively.
16. A disclaimer of opinion was issued on the prior year's financial statements. I was unable to determine the extent of the effect of these limitations on the balances as at 30 June 2012.

### **Provisions**

17. In terms of GRAP 19, *Provisions, Contingent Liabilities and Contingent Assets*, a provision shall be the best estimate of the expenditure required to settle the present obligation at the reporting date. The provision for the landfill site was not adequately determined at year-end. Management prepared an estimate four months after year-end and could not satisfactorily indicate how the timing difference between year-end and the preparation date was considered in preparing the estimate. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that provisions had been properly recorded. Therefore, I could not rely on the validity and accuracy of the landfill site rehabilitation provision amounting to R3 296 273 (2011: R2 796 273), as disclosed in note 17 to the financial statements.

### **Distribution losses**

18. Section 125(2)(d)(i) of the MFMA states that the notes to the annual financial statements of a municipality must disclose particulars of any material losses. The municipality did not disclose distribution losses with regard to water, as the municipality had not implemented adequate control measures to reliably calculate these losses. I was unable to determine the total extent of the understatement of distribution losses, as sufficient appropriate audit evidence could not be obtained. There were no satisfactory alternative audit procedures that I could perform to obtain reasonable assurance that material losses had been properly recorded.

### **Aggregation of immaterial uncorrected misstatements**

19. The financial statements as a whole were materially misstated due to the cumulative effect of numerous individually immaterial uncorrected misstatements in the following elements making up the statement of financial position, the statement of financial performance and the notes to the financial statements:
  - Revenue reflected as R221 390 289 is understated by R1 303 664.
  - Expenditure reflected as R150 652 421 is understated by R3 581 158.
  - Employee cost reflected as R56 569 772 is understated by R840 103.
  - Finance costs reflected as R875 370 are understated by R110 934.
  - Consumer debtors reflected as R33 026 742 are understated by R447 843.
  - Finance leases reflected as R302 740 are overstated by R263 452.
  - Property, plant and equipment reflected as R697 837 063 is overstated by R339 305.
  - Trade and other payables reflected as R31 602 399 are overstated by R2 044 730.
  - The accumulated surplus reflected as R775 529 120 is understated by R479 745.

### **Qualified opinion**

20. In my opinion, except for the effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Umjindi Local Municipality as at 30 June 2012 and its financial performance and cash flows for the year then ended, in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA.

### **Additional matter**

21. I draw attention to the matter below. My opinion is not modified in respect of this matter.

### **Unaudited supplementary schedules**

22. The supplementary information set out on pages 58 to 63 and 66 to 67 does not form part of the financial statements and is presented as additional information. I have not audited this schedule and, accordingly, I do not express an opinion thereon.

## **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

23. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

### **Predetermined objectives**

24. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages xx to xx of the annual report.
25. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned development priorities or objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).
26. The reliability of the information in respect of the selected development priorities is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).
27. The material findings are as follows:

### **Usefulness of information**

### **Presentation**

28. Improvement measures were not disclosed in the annual performance report for any of the planned targets not achieved, as required by section 46 of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA). This was due to inadequate internal policies and procedures over the processes pertaining to the reporting of performance information.

## **Consistency**

29. Section 41(c) of the MSA requires that the annual performance plan should form the basis for the annual report, therefore requiring the consistency of objectives, indicators and targets between planning and reporting documents. A total of 76% of the reported indicators were not consistent with the indicators as per the approved annual performance plan. This was due to a lack of management planning and review.

## **Measurability**

30. The FMPPI requires that the time period or deadline for delivery should be specified. A total of 96% of the targets relevant to the develop sustainable infrastructure for service delivery for water, sanitation, roads and storm water, electricity and social amenities as well as promote sustainable social development programmes were not time bound in specifying a time period or deadline for delivery. This was due to the fact that management was aware of the requirements of the FMPPI but had not received the necessary training to enable application of the principles.

## **Reliability of information**

### **Validity**

31. The FMPPI requires that processes and systems that produce the indicator should be verifiable. A total of 43% of the actual reported performance relevant to the selected development priority differed materially when compared to the source information or evidence provided. This was due to a lack of monitoring and review of the recording of actual achievements by senior management.

### **Accuracy**

32. The FMPPI requires that the indicator be accurate enough for its intended use and respond to changes in the level of performance. A total of 43% of the actual reported indicators relevant to the develop sustainable infrastructure for service delivery and strengthen the delivery of basic services programmes were not accurate when compared to the source information. This was due to a lack of monitoring and review of the recording of actual achievements by senior management.

### **Completeness**

33. The FMPPI requires that documentation addressing the systems and processes for identifying, collecting, collating, verifying and storing information should be properly maintained. I was unable to obtain all the information and explanations I considered necessary to satisfy myself as to the completeness of the actual reported performance relevant to 36% of the develop sustainable infrastructure for service delivery and strengthen the delivery of basic services programmes. This was due to limitations placed on the scope of my work by the absence of information systems. The municipality's records did not permit the application of alternative audit procedures.
34. The FMPPI requires that documentation addressing the systems and processes for identifying, collecting, collating, verifying and storing information should be properly maintained. The municipality could not provide sufficient appropriate evidence to support any of the selected development objectives.

## **Additional matter**

35. I draw attention to the matter below. This matter does not have an impact on the audit findings on predetermined objectives reported above.

## **Achievement of planned targets**

36. Of the 380 planned targets, only 53 were achieved during the year under review. This means that 86% of the total planned targets were not achieved during the year under review. This was mainly due to the fact that indicators and targets were not suitably developed during the strategic planning process.

## **Compliance with laws and regulations**

37. I performed procedures to obtain evidence that the entity has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the general notice issued in terms of the PAA are as follows:

## **Annual financial statements, performance report and annual report**

38. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets and provisions identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided. However, the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

## **Expenditure management**

39. Money owing by the municipality was not always paid within 30 days of receiving an invoice or statement, as required by section 65(2)(e) of the MFMA.
40. The accounting officer did not take effective steps to prevent irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

## **Asset and liability management**

41. An adequate management, accounting and information system was not in place to account for assets, as required by section 63(2)(a) of the MFMA.

## **Procurement and contract management**

42. In contravention of section 12(3) of the SCM policy, the municipality deliberately split orders for goods and services to avoid the requirement of competitive bidding. Deviations were not approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM Regulation 36(1).
43. Invitations for competitive bidding were not always advertised for the required minimum period, as required by SCM Regulation 22(1) and (2).
44. The performance of contractors and providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA.

45. A list of accredited prospective providers was not in place for procuring goods and services through quotations, as required by SCM Regulation 14(1)(a).
46. The prospective providers' list for procuring goods and services through quotations was not updated at least quarterly to include new suppliers that qualify for listing, and prospective providers were not invited to apply for such listing at least once a year, as per the requirements of SCM Regulation 14(1)(a)(ii) and (2).
47. Contracts and quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM Regulation 13(c).

#### **Revenue management**

48. An adequate management, accounting and information system was not in place to recognise revenue when it was earned, as required by section 64(2)(e) of the MFMA.

#### **Internal control**

49. I considered internal control relevant to my audit of the financial statements, the annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for the qualified of opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

#### **Leadership**

50. Management did not exercise oversight responsibility regarding financial and performance reporting and compliance as well as related internal controls.
51. The municipality did not adequately review the financial statements and the annual performance report prior to their submission for auditing and thus significant matters that required the adjustment of the financial statements were not identified and corrected.
52. The municipality did not have documented and approved internal policies and procedures to address the process of collection, recording, processing, monitoring and reporting performance information.
53. The municipality did not implement and action plan to address the findings on performance information.

#### **Financial and performance management**

54. Management did not implement proper record keeping in a timely manner to ensure that complete, relevant and accurate information was accessible and available to support financial and performance reporting.
55. Management did not prepare regular, accurate and complete financial and performance reports that were supported and evidenced by reliable information.
56. Management did not perform adequate reconciliation for property, plant and equipment as evidenced by misstatements.

57. The financial statements contained misstatements. This was mainly due to lack of adequate reviews by management.

58. Non-compliance with laws and regulations relating to supply chain management and MFMA could have been prevented had compliance been properly reviewed and monitored.

#### **Governance**

59. Management did not ensure that there was an adequately resourced and functioning internal audit unit that identified internal control deficiencies and recommended corrective action effectively.

*AUDITOR-GENERAL*

Nelspruit

14 December 2012



AUDITOR-GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*